

PUBLIC UTILITIES COMMISSION

505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102-3298



March 10, 2005

Agenda ID #4389
Ratesetting

TO: PARTIES OF RECORD IN APPLICATION 03-08-004

This is the draft decision of Administrative Law Judge (ALJ) Wong. It will not appear on the Commission's agenda for at least 30 days after the date it is mailed. The Commission may act then, or it may postpone action until later.

When the Commission acts on the draft decision, it may adopt all or part of it as written, amend or modify it, or set it aside and prepare its own decision. Only when the Commission acts does the decision become binding on the parties.

Parties to the proceeding may file comments on the draft decision as provided in Article 19 of the Commission's "Rules of Practice and Procedure." These rules are accessible on the Commission's website at <http://www.cpuc.ca.gov>. Pursuant to Rule 77.3 opening comments shall not exceed 15 pages. Finally, comments must be served separately on the ALJ and the assigned Commissioner, and for that purpose I suggest hand delivery, overnight mail, or other expeditious method of service.

/s/ ANGELA K. MINKIN
Angela K. Minkin, Chief
Administrative Law Judge

ANG:sid

Attachment

Decision **DRAFT DECISION OF ALJ WONG** (Mailed 3/10/2005)

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Pacific Gas and Electric Company
for Adoption of its 2004 Energy Resource
Recovery Account (ERRA) Forecast Revenue
Requirement, for Review of Contract
Administration, Least Cost Dispatch and
Procurement Activities during the Record Period
January 1, 2003, Through May 31, 2003, and for
Approval of its 2004 Ongoing Competition
Transition Charges (CTC) Revenue Requirement
and Proposed Rate Design. (U 39 E)

Application 03-08-004
(Filed August 1, 2003)

**OPINION REGARDING THE JANUARY 1, 2003 THROUGH MAY 31, 2003
RECORD REVIEW PERIOD**

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**OPINION REGARDING THE JANUARY 1, 2003 THROUGH MAY 31, 2003
RECORD REVIEW PERIOD**

I. Summary

On August 1, 2003, Pacific Gas and Electric Company (PG&E) filed its application for the adoption of its 2004 Energy Resource Recovery Account (ERRA) revenue requirement forecast, for review of its contract administration, least cost dispatch and procurement activities for the five-month record period of January 1, 2003 through May 31, 2003, and for approval of its proposed 2004 rates for the ongoing Competition Transition Charge (CTC).¹

This decision addresses the ERRA activities associated with the five-month record review period. The decision finds that PG&E's activities concerning contract administration, least cost dispatch, procurement activities, and generation fuel costs were in compliance with PG&E's 2003 updated procurement plan and related decisions. This decision also concludes that PG&E is entitled to recover the costs associated with these activities to the extent existing rates do not fully recover these costs.

¹ In Decision (D.) 04-06-012 we adopted, on an interim basis, a 2004 ERRA revenue requirement of \$2.189 billion, and a 2004 ongoing CTC revenue requirement of \$144.026 million. D.04-06-012 noted that these amounts could change depending on how the litigated CTC issues were resolved. In D.05-01-031, we addressed the CTC issues and adopted, without change, the interim ERRA and CTC revenue requirements set in D.04-06-012.

II. Procedural History

In D.02-10-062, the Commission ordered PG&E to submit an updated 2003 short-term procurement plan. D.02-10-062 also established the ERRA balancing account to record and recover PG&E's energy procurement plan power costs.² The ERRA records the authorized ERRA revenue requirement and actual power costs to determine PG&E's recovery of its power costs, excluding the costs associated with the California Department of Water Resources (DWR) power contracts. PG&E's updated procurement plan was approved in D.02-12-074.

In D.03-10-059, the decision addressing PG&E's forecast of its 2003 ERRA revenue requirement, we approved a stipulation between PG&E and the Office of Ratepayer Advocates (ORA) that allowed PG&E to include its 2004 ERRA forecast and its ERRA reasonableness showing for the first five months of 2003 in its August 1, 2003 ERRA filing.³ PG&E filed the above-captioned application on August 1, 2003. This is the first review of PG&E's ERRA-related activities.

Following the prehearing conference, the February 3, 2004 scoping memo and ruling determined that three days of evidentiary hearings should be reserved in May 2004 to litigate possible issues associated with the five-month record period. At a prehearing conference held on May 3, 2004, PG&E and ORA agreed that the May 2004 evidentiary hearings were not needed, and that ORA's need for additional data in future ERRA filings could be handled through a

² D.02-10-062 was modified in part by D.02-12-074.

³ Originally, the review period in this proceeding was for the first five months of 2003. PG&E filed a motion on March 17, 2004 to have the remaining seven months of 2003 reviewed in this proceeding. PG&E's motion was granted in an April 16, 2004 Administrative Law Judge's (ALJ) ruling.

master data request. PG&E and ORA also agreed that briefs should be filed on the issue of how broad the scope of the ERRA review should be. A briefing schedule was established.

The testimony regarding the five-month record review period is composed of PG&E's redacted and unredacted testimony dated August 1, 2003, ORA's unredacted and redacted testimony dated April 9, 2004, ORA's errata to Chapter 4 of ORA's testimony dated April 19, 2004, and PG&E's rebuttal testimony dated April 26, 2004. These five pieces of testimony were received into evidence at the prehearing conference as Exhibits 100 to 105, respectively.

Opening briefs on the scope of the ERRA review were filed by PG&E and ORA on May 27, 2004, and reply briefs were filed by PG&E and ORA on June 24, 2004.

III. Introduction to the ERRA Review

A. Position of the Parties

1. PG&E

PG&E's testimony regarding the five-month record period consists of Exhibits 100, 101, and 105. Exhibit 101 is the unredacted version of Exhibit 100. Exhibits 100 and 101 describe PG&E's 2003 procurement plan, least cost dispatch processes, contract administration, procurement activities, and generation fuel costs. Exhibit 105 responds to ORA's testimony, the scope of review for least cost dispatch, and ORA's recommendation that certain data and information be provided in future ERRA filings.

PG&E asserts its exhibits demonstrate "that its contract administration and least-cost dispatch activities [for the five-month record review period] were in full compliance with the requirements of Public Utilities Code Section 454.5," and that it acted "reasonably and made appropriate

dispatch decisions at all times during the record period.” (PG&E, Opening Brief, pp. 2, 3.)⁴

ORA was the only party to actively participate in the five-month record review phase of this proceeding, and the only party to submit responsive testimony. Since PG&E filed its application, it has met “with ORA staff over 10 times to explain the process and demonstrate the tools PG&E has in place to manage and dispatch the portfolio of available resources,” and has “promptly and fully responded to all of ORA’s written and oral requests for information.” (PG&E, Opening Brief, p. 2.)

PG&E recommends that the Commission find the following:

“There are no factual disputes;

“There is no recommendation for disallowance or a finding of unreasonableness in ORA’s testimony;

“PG&E provided all data that was requested; and

“PG&E’s activities for this record period should be found to be in compliance with its Procurement Plan and that the record period review should be closed.” (Ex. 105, pp. 1-2.)

2. ORA

ORA’s testimony for the five-month record review period consists of Exhibits 102, 103, and 104. Exhibits 102 and 103 are the unredacted and redacted “Report on Reasonableness Review” of PG&E’s ERRAs, respectively. Exhibit 104 is an errata to Chapter 4 of Exhibits 102 and 103. ORA reviewed PG&E’s contract

⁴ All code section references are to the Public Utilities Code.

administration, retained generation fuel expenses, and least cost dispatch for the five-month record period.

ORA does not recommend any disallowances in this ERRA review because it is unclear what the scope of review for least cost dispatch and the standard of review should be. Until the Commission resolves these two issues, ORA states that “ongoing and future ERRA reviews will continue to falter as parties disagree on the fundamental purpose of these proceedings.” (ORA, Reply Brief, p. 2.) Since procurement costs amount to billions of dollars, ORA asserts the Commission must clarify the scope of review and standard of review.

Since this is the first review of the ERRA since PG&E resumed procurement responsibilities on January 1, 2003, ORA is still “developing the most efficient and effective method for reviewing utility contract administration and least cost dispatch.” (Exhibits 102 and 103, p. 1-1.) To enhance the review of future ERRA filings and to better understand PG&E’s contract administration and least cost dispatch processes, ORA originally recommended that PG&E be ordered to provide specific data and information as described in Exhibits 102 and 103, and that ORA be given additional time to develop a meaningful framework for evaluating least cost dispatch and contract administration for all three electric utilities. ORA subsequently noted in its opening and reply briefs that PG&E agreed to work with ORA on the type of data and information that PG&E will provide in future ERRA reviews, and to develop a master data request for use in future ERRA reviews.

ORA requests that the Commission address the following in its decision:

“(1) Confirm that a reasonableness review is the appropriate standard of review for contract administration, least cost dispatch, and URG [utility retained generation];

(2) Confirm that, while AB [Assembly Bill] 57 eliminates after-the-fact reasonableness reviews for a contract’s terms, a reasonableness review is appropriate for URG, contract administration, and least cost dispatch; and

(3) Confirm that the scope of review for least cost dispatch includes (i) all of PG&E’s portfolio resources and (ii) any decisions, actions and estimates made by PG&E, even as long as a year before the dispatch day.” (ORA, Reply Brief, pp. 5-6.)

B. Discussion

The ERRA balancing account was established in D.02-10-062 to track actual recorded energy procurement costs against the authorized energy procurement costs in the revenue requirement. PG&E’s 2003 ERRA revenue requirement of \$1.373 billion was adopted in D.03-10-059.

Today’s decision is the first review of PG&E’s ERRA activities since it resumed procuring energy for its customers. ORA reviewed PG&E’s ERRA-related activities for the five-month record period of January 1, 2003 through May 31, 2003. ORA did not recommend any disallowances or findings

of unreasonableness.⁵ ORA believes, however, that the Commission should address the scope of review for least cost dispatch and the standard of review so as to provide guidance for future ERRA reviews. ORA raised the same issue in Southern California Edison Company's (SCE) ERRA review application in Application (A.) 03-10-022, and which the Commission decided in D.05-01-054.

Although the scope and standard of review are an integral part of the ERRA review, ORA does not take issue with PG&E's ERRA-related activities for the first five months of 2003. Before addressing the ERRA-related activities, we first address the scope of review for least cost dispatch and the standard of review. After that, we address PG&E's contract administration, procurement, and least cost dispatch for the record period.

IV. Scope of Review

A. Position of the Parties

1. PG&E

PG&E contends that the Commission already addressed the scope of review for least cost dispatch in previous decisions and that this issue should not be revisited in this proceeding. Since PG&E's position about the scope of review for least cost dispatch is closely tied to its position regarding the standard of review, PG&E's position on both issues is summarized in the paragraphs which follow.

⁵ With respect to the contract administration of the non-QF contracts, ORA states that based on the information provided by PG&E, "ORA cannot determine whether its contract administration is reasonable." (Ex. 102, p. 3-8.)

PG&E contends that the Legislature's enactment of AB 57, which added § 454.5,⁶ was intended to eliminate after-the-fact reasonableness reviews. In support of that intent, PG&E's opening brief attached an April 28, 2004 letter from the Governor to President Peevey regarding the electricity market structure.⁷ In that letter the Governor wrote: "AB 57 corrected one of the key flaws in California's restructuring effort: the inability of investor-owned utilities to develop diversified resource portfolios and enter into long-term contracts without the risk of after-the-fact reasonableness reviews by the Commission." (PG&E, Opening Brief, p. 6, Attachment.)

PG&E cites to various portions of § 454.5 in support of its position. Section 454.5(d)(2) states in part that one of the objectives of a Commission-approved procurement plan is to "Eliminate the need for after-the-fact reasonableness reviews of an electrical corporation's actions in compliance with an approved procurement plan, including resulting electricity procurement contracts, practices, and related expenses." (PG&E, Opening Brief, p. 5; Pub. Util. Code § 454.5(d)(2).) PG&E contends that this sentence was intended by the Legislature to eliminate after-the-fact reasonableness reviews and to replace them with compliance reviews "to verify and assure that the utility acted in compliance with its approved procurement plan." (PG&E, Reply Brief, p. 3.) PG&E asserts that this compliance review standard is set forth in D.02-10-062 wherein the Commission stated "The utilities shall prudently administer all contracts and generation resources and dispatch the energy in a least-cost

⁶ See Stats. 2002, ch. 835, § 2, and Stats. 2002, ch. 850, § 3.

⁷ PG&E requests that judicial notice be taken of the Governor's letter.

manner.” (PG&E, Reply Brief, pp. 3-4; D.02-10-062, pp. 52, 74.) According to PG&E, this allows the Commission to verify that the contracts were administered in accordance with their terms and whether contract disputes were reasonably resolved.

PG&E also states that § 454.5(h) does not alter or change “the commission’s oversight of affiliate transactions under its rules and decisions or the commission’s existing authority to investigate and penalize an electrical corporation’s alleged fraudulent activities, or to disallow costs incurred as a result of gross incompetence, fraud, abuse, or similar grounds.” (PG&E, Opening Brief, pp. 5-6; Reply Brief, pp. 1-2; Pub. Util. Code § 454.5(h).)⁸

PG&E also cites excerpts from D.02-10-062, D.02-12-069, D.02-12-074, D.03-06-067, D.03-06-074, D.03-06-076, and D.03-10-090 in support of its contention that the Commission has already addressed the permissible scope of ORA’s review.

Since ORA has not alleged that PG&E’s actions were out of compliance with the adopted 2003 procurement plan, and PG&E has not objected to any of ORA’s requests for information, PG&E contends there is no need to address the scope of review of least cost dispatch in this proceeding because there is no actual controversy. PG&E contends that ORA is seeking an advisory opinion, which the Commission has been reluctant to issue if there is no controversy before the Commission.

If the Commission intends to address the scope of review, PG&E states that this proceeding should be coordinated with SCE’s ERRR proceeding in A.03-10-022. ORA and SCE have disagreed on the scope of the ERRR review in that proceeding. According to PG&E, ORA’s position in A.03-10-022 is “that

⁸ PG&E contends that since AB 57 specifically identified an area where the Commission’s current jurisdiction to investigate and take action was not affected by the legislation, that by implication, the Legislature “fully intended to limit the Commission’s jurisdiction in other ways involving review of electricity procurement.” (PG&E, Reply Brief, p. 2.)

the review should be a full-blown reasonableness review, and should be called a reasonableness review,” while SCE’s position is that it should be called a compliance review. (PG&E, Opening Brief, p. 12.) PG&E asserts that SCE’s position “better reflects the statutory and Commission intent.” (*Ibid.*)

PG&E asserts that the scope of a compliance review is to determine whether a utility’s actions were in compliance with its approved procurement plan, including the least-cost dispatch standard enunciated in what has become known as Standard of Conduct (SOC) 4 in D.02-10-062. According to PG&E, the compliance review should review the following three categories:

“1) review of utility dispatch of resources and contracts to ensure least cost dispatch; 2) confirmation that procurement contracts were administered in accordance with their terms; and 3) review of transactions that through the quarterly transaction report confirmation procedure have been determined to be ‘outside’ an approved procurement plan.” (PG&E, Opening Brief, p. 12.)

PG&E contends that under the first category, “it is clear that the Commission does not have authority to conduct a reasonableness review of the terms and conditions of a procurement transaction that was in conformance with the utility’s approved procurement plan.” (PG&E, Opening Brief, p. 12.) PG&E asserts that the transactions or resources cannot be questioned or second-guessed, and that the only issue is whether the components of the utility’s portfolio were dispatched on a least cost basis.

For the second category, PG&E asserts that “the Commission may verify that the utility, in its administration of procurement contracts, did so in accordance with the terms of such contracts and appropriately settled any

contract administration disputes with the counter party.” (PG&E, Opening Brief, p. 13.)

For category three, PG&E asserts that if a transaction has been identified in the quarterly transaction filing process as not being in compliance with an approved procurement plan, and the transaction has not been approved in an advice letter filing or in an application for pre-approval, the Commission may review the transaction for reasonableness since it is not covered by an approved procurement plan.

PG&E contends that the principles that apply to the scope of a compliance review are already contained in the language of the seven decisions cited earlier. If the Commission finds that there is a need to address the scope of review again, the Commission should be consistent with the prior decisions. PG&E asserts that it has fully complied with the scope of review for least-cost dispatch in this proceeding.

2. ORA

ORA contends that “the Commission is permitted to review as much information as it deems necessary to evaluate the reasonableness of PG&E’s costs related to least cost dispatch.” (ORA, Reply Brief, p. 5.) ORA asserts that neither AB 57 nor the Commission’s decisions have limited this scope of review. ORA contends that until the Commission puts specific boundaries on the scope of this analysis, the scope of review of least cost dispatch includes “all decisions, actions and estimates made by PG&E, even as long as a year before the dispatch day.” (ORA, Reply Brief, p. 5.) ORA states that D.03-06-076, D.03-06-067, and “other Commission decisions are unclear as to how far back one can examine records and dispatch data in order to determine the reasonableness of dispatch decisions during the Record Period.” (Exhibits 102 and 103, p. 1-2.)

ORA agrees with PG&E that AB 57 identified certain procurement costs that are not subject to reasonableness review, such as the terms of the procurement contracts and their pricing provisions. Although AB 57 does not allow the Commission to review the reasonableness of the contract terms, it does allow the Commission to review the utility's implementation of those same contract terms, and the utility's management and implementation of its procurement plans. ORA points out that this distinction is addressed in D.03-06-067 at page 10, and in D.03-10-090 at page 5.

In order to determine whether PG&E optimized its overall procurement portfolio, ORA contends that it must review the utility's entire resource portfolio under the least cost dispatch principles. ORA cites the following passage from D.03-06-074 in support of its position:

“The utilities and the Commission have different interpretations of procurement legislation, particularly AB 57, section 1(d), which states that it is the Legislature's intent to: ‘(d) Direct the Public Utilities Commission to assure that each electrical corporation optimizes the value of its overall supply portfolio, including Department of Water Resources contracts and procurement pursuant to Section 454.5 of the Public Utilities Code, for the benefit of its bundled service customers.’ Consistent with this language, the Commission views AB 57, section 1(d) as linking Section 454.5 to the Commission's legislative mandate to optimize overall supply portfolios, including DWR's. [Footnote omitted.] In fulfilling this mandate, the Commission is required to review the reasonableness of the utilities' administration of DWR contracts, and require the utilities to perform least cost dispatch to optimize existing resources and reduce costs to ratepayers.” (ORA, Opening Brief, p. 8; D.03-06-074 at p. 7.)

In D.03-10-090, the Commission said that AB 57 “does not prohibit review for least cost dispatch because the focus of the statute is procurement transactions and contracts, rather than the management of those contracts.” (D.03-10-090, p. 5.)

ORA asserts that its interpretation of the Commission’s scope of review is consistent with ensuring that PG&E has optimized its supply portfolio. If ORA cannot review all of the resources in PG&E’s portfolio, ORA contends it cannot determine if PG&E complied with the Commission’s directive to optimize the value of its overall portfolio. ORA requests that the Commission “confirm that the scope of the least cost dispatch analysis includes (1) all of PG&E’s portfolio resources and (2) any decisions, actions, and estimates made by PG&E, even as long as a year before the dispatch day.” (ORA, Opening Brief, pp. 8-9.)

B. Discussion

Least cost dispatch, which has been mentioned in various decisions,⁹ is best described by the following excerpt from D.02-12-074, as modified by D.03-06-076:

“Prudent contract administration includes administration of all contracts within the terms and conditions of those contracts, to include dispatching dispatchable contracts when it is most economical to do so. In administering contracts, the utilities have the responsibility to dispose of economic long power and to purchase economic short power in a manner that minimizes ratepayer costs. Least-cost dispatch refers to a situation in which the most cost-effective mix of total resources is used, thereby minimizing the cost of

⁹ See D.02-09-053, pp. 6, 38-39, 65-66; D.02-10-062, pp. 52, 74; D.02-12-069, pp. 64, 70; D.02-12-074, p. 54; and D.03-06-076, p. 23.

delivering electric services. The utility bears the burden of proving compliance with the standard set forth in its plan.” (D.02-12-074, p. 54; D.03-06-076, pp. 46-47.)

PG&E believes that since there is no actual controversy in this proceeding regarding least cost dispatch, that there is no need to address the scope of review of least cost dispatch at this time. PG&E's position is that the Commission's adoption of an approved procurement plan with upfront standards eliminates the need for an after-the-fact reasonableness review of the utility's actions with respect to the administration of transactions and contracts entered into during the record period. Since no reasonableness review is needed, the information to be reviewed by ORA concerning least cost dispatch decisions should be limited. Thus, in determining whether a utility's portfolio was dispatched on a least cost basis, PG&E appears to advocate that the information about least cost dispatch be limited to events that coincide with the dispatch decision.¹⁰

ORA, on the other hand, takes the position that AB 57 and the decisions which interpreted those statutory provisions, has not limited "how far back one can examine records and dispatch data in order to determine the reasonableness of dispatch decisions during the Record Period." (Exhibits 102 and 103, p. 1-2.) ORA takes the position that the review of least cost dispatch should look at "the entire time period that all short term procurement decisions and actions were made that impacted the dispatch day." (Exhibits 102 and 103, p. 2-3.)

¹⁰ In footnote 1 of PG&E's reply brief, PG&E states that "The only area where PG&E has tried to limit the scope of data given to ORA has been an attempt to limit data to information pertaining to or relevant to the time frame of the record period." PG&E also notes that "ORA has generally been agreeable to this limitation."

It is appropriate to address the scope of review of least cost dispatch in this decision so that PG&E and ORA have guidance in future ERRA proceedings regarding the review of PG&E's dispatch activities.

This dispute over the scope of review of least cost dispatch in ERRA proceedings was recently addressed by us in A.03-10-022, SCE's 2004 ERRA revenue requirement proceeding. In D.05-01-054, we concluded that "Least-cost dispatch review in the ERRA should include SCE's decisions to dispatch the resources under its control in the daily, hourly and real-time markets." (D.05-01-054, p. 36, COL 2.)¹¹ We reached this conclusion based on prior Commission decisions and § 454.5.

The starting point for our analysis of the scope of review for least cost dispatch is § 454.5, which was added to the Public Utilities Code by AB 57. Section 454.5 addresses the energy procurement plan that is filed with the Commission. Pursuant to § 454.5(d)(2), the procurement plan that is approved by the Commission shall accomplish, among other things, the following:

"Eliminate the need for after-the-fact reasonableness reviews of an electrical corporation's actions in compliance with an approved procurement plan, including resulting electricity procurement contracts, practices, and related expenses. However, the commission may establish a regulatory process to verify and assure that each contract was administered in accordance with the terms of the contract,

¹¹ SCE took the position in A.03-10-022 that only spot market transactions (day ahead, hour ahead and real-time) should be included in ORA's review of least cost dispatch. ORA took the position that the review should include "the decisions, actions, and estimates made by the utility as long as a year before the dispatch day, as well as month-ahead, week-ahead, day ahead and possibly hour ahead decisions." (D.05-01-054, p. 6.)

and contract disputes which may arise are reasonably resolved.”

Section 454.5(b) described what the utility's proposed procurement plan must contain. Among the provisions to be included in the procurement plan are "upfront standards and criteria by which the acceptability and eligibility for rate recovery of a proposed procurement transaction will be known by the electrical corporation prior to execution of the transaction." (Pub. Util. Code § 454.5(b)(7).)

The Commission adopted "upfront standards and criteria" when it addressed the "minimum standards of conduct and restrictions on affiliate transactions" in D.02-10-062. (D.02-10-062, pp. 51-52, 79, OP 15.) In what has become known as SOC 4, the Commission adopted the following:

"The utilities shall prudently administer all contracts and generation resources and dispatch the energy in a least-cost manner. Our definitions of prudent contract administration and least cost dispatch are the same as our existing standard." (D.02-10-062, p. 52.)

In D.02-12-074, we elaborated on SOC 4. We stated in part:

"Prudent contract administration includes administration of all contracts within the terms and conditions of those contracts, to include dispatching dispatchable contracts when it is most economical to do so. In administering contracts, the utilities have the responsibility to dispose of economic long power and to purchase economic short power in a manner that minimizes ratepayer costs." (D.02-12-074, p. 54.)

D.02-12-074 also clarified that "in determining whether utilities have dispatched resources in compliance with their plans' requirements, contract terms or prices will not be at issue." (D.02-12-074, p. 54.)

As noted in D.05-01-054, D.03-10-090, and D.02-12-074, SOC 4 “is the upfront standard in a utility’s procurement plan regarding prudent contract administration and energy dispatch decisions.” (D.05-01-054, p. 8; D.03-10-090, p. 5; D.02-12-074, p. 54.) Since least cost dispatch is part of the contract administration, SOC 4 does not allow the Commission to conduct an after-the-fact reasonableness review of the terms or prices of the contracts.¹² (D.03-06-076, pp. 24-25.) However, as explained in D.03-06-076:

“Least-cost dispatch is an up-front standard that is included in the procurement plans. Any subsequent review of dispatch merely ensures that the utilities have complied with the approved procurement plans. Nothing in section 454.5 prohibits the Commission’s review of utility actions to determine whether the utility complied with an approved procurement plan. Indeed, the statute [§ 454.5(d)(2)] states that a procurement plan shall eliminate the need for after-the-fact reasonableness reviews of a utility’s actions *in compliance* with an approved procurement plan. (D.03-06-076, p. 25.)

Since a review of least cost dispatch is permitted, the remaining issue is how much information should be reviewed. In D.05-01-054, we held that “SCE’s decisions to dispatch the resources under its control in the daily, hourly and real-time markets is relevant for review in ERRRA filings,” and that “forward purchase and sale transactions done months prior to the time of dispatch are considered procurement activities and as such, should be reviewed in the quarterly compliance Advice Letter filings.” (D.05-01-054, p. 9.)

¹² Since after-the-fact reasonableness review is prohibited by the express language in § 454.5(d)(2), there is no need to take official notice of the Governor’s April 28, 2004 letter.

In this proceeding, ORA believes that “least cost dispatch is to determine whether the utility, while complying with the utility’s procurement plan, selected the resources to meet its load and other requirements in a least cost manner over the entire time period that all short term procurement decisions and actions were made that impacted the dispatch day.” (Ex. 102, p. 2-3.) ORA contends that this “entire time period” covers “decisions, actions and estimates made by PG&E, even as long as a year before the dispatch day,” and that the scope of review of least cost dispatch includes “all of PG&E’s portfolio resources.”

Unlike SCE’s position in D.05-01-054, PG&E does not assert that least cost dispatch review is limited to spot market transactions, i.e., day-ahead, hour-ahead and real-time purchases and sales. (See D.05-01-054, p. 9.) However, PG&E does note in its opening brief that the quarterly compliance advice letter sets forth a process “for reviewing the products purchased, transaction types, and contract terms and prices” which detail “all transactions in compliance with the approved plan.” (PG&E, Opening Brief, p. 13, fn. 3.)

We will apply the same scope of review of least cost dispatch to PG&E’s ERRR proceedings, as we have adopted for SCE’s ERRR proceedings. Accordingly, PG&E’s decisions to dispatch the resources under its control in the daily, hourly and real-time markets are relevant to the ERRR review. The forward purchase and sale transactions that are done months prior to the time of dispatch should be considered procurement activities and should be reviewed in the quarterly compliance advice letter filings. (See D.05-01-054, p. 9.)

V. Standard of Review**A. Position of the Parties**

PG&E's position regarding the standard of review has been described in the scope of review section above.

ORA takes the position that the standard of review needs to be addressed in this proceeding because it determines the level of scrutiny that should be given to PG&E's procurement costs. ORA asserts that PG&E has mixed the scope of review issue with the standard of review issue, and that PG&E fails to directly address what the appropriate standard of review should be in an ERRA review.

ORA contends that AB 57 did not "eliminate the Commission's authority to engage in reasonableness reviews of all procurement costs." (ORA, Opening Brief, p. 3, fn. 1.) In § 454.5(d)(2), the Commission was authorized to establish a regulatory process to verify that each contract is administered in accordance with the terms of the contract. ORA contends that this regulatory process allows it to "engage in the type of review typically referred to as a 'reasonableness review.'" (ORA, Opening Brief, p. 3, fn. 1.)

PG&E claims that according to the language in § 454.5(h), the Commission cannot find PG&E's procurement costs unreasonable unless the actions of PG&E amount to gross incompetence, fraud, or abuse. ORA asserts that PG&E's interpretation of this subdivision is wrong, and that the Commission considered and rejected such an interpretation in D.02-12-069. ORA points out that in D.02-12-069 the Commission stated that "Under SCE's proposed standard the utilities' administration of the contracts would be deemed reasonable absent evidence of gross negligence, of involved intentional misconduct, fraud, or a knowing violation of the law." (D.02-12-069, p. 60.) The

Commission further stated that “We will retain the existing ‘reasonable manager’ standard adopted in D.02-10-062,” and will also consider certain factual circumstances surrounding the utilities’ procurement circumstances. (D.02-12-069, p. 61.)

ORA also asserts that the reference in § 454.5(d)(5) to “just and reasonable rates, with an appropriate balancing of price stability and price level in the electrical corporation’s procurement plan” supports ORA’s belief that AB 57 specifically contemplates reasonableness reviews for the ERRA reviews.

ORA further asserts that the standard of review for utility procurement-related costs is found in D.02-10-062. In SOC 4, it states that the “utilities shall prudently administer all contracts and generation resources and dispatch the energy in a least-cost manner.” SOC 4 also states that “Our definitions of prudent contract administration and least cost dispatch is the same as our existing standard.” (D.02-10-062, p. 52.)

ORA contends that the “existing standard” can be found in prior decisions that addressed the utilities’ responsibilities under the servicing agreements with DWR, and that this existing standard is a reasonableness review. Based on D.02-09-053, ORA asserts that the level of review for contract administration and least cost dispatch is not a simple “compliance review,” as PG&E suggests. Instead, Commission precedent points to reasonableness review as the appropriate level of scrutiny of procurement-related costs.

ORA contends that the reasonable manager standard in D.02-10-062 should be used to review the reasonableness of the procurement costs. D.02-10-062 was adopted in response to the abuses of the energy companies during the energy crises. The Commission stated that the “magnitude of these abuses clearly affirms the need for strong standards and vigilant oversight of

energy procurement practices and the need for the Commission to investigate and act at any time if standards are violated.” (D.02-10-062, p. 50; PG&E, Opening Brief, pp. 5-6.) ORA asserts that PG&E’s use of a gross incompetence standard is inconsistent with the Commission’s efforts to protect the California electricity market, and would result in the Commission’s abdication of its authority to review the reasonableness of procurement costs, which amount to billions of dollars.

With respect to URG costs, ORA notes that in D.02-10-062 the Commission named the ERRA proceedings as the forum for reviewing the reasonableness of URG. D.02-10-062 stated that “We will use the semiannual applications ... to review the reasonableness of URG expenses, contract administration, and least-cost dispatch operations....” (ORA, Opening Brief, p. 9; D.02-10-062, p. 65.) ORA asserts that PG&E does not contest this, and the Commission should therefore confirm that reasonableness review is the appropriate standard of review for URG costs.

B. Discussion

ORA takes the position that SOC 4 enunciated that the appropriate standard of review “is the same as our existing standard,” which is a reasonableness review. ORA asserts that the reasonableness review should apply to least cost dispatch and to contract administration. PG&E asserts that AB 57 eliminated reasonableness reviews, and that the type of review contemplated by AB 57 is a “compliance review.”

We addressed the standard of review in D.05-01-054, SCE’s ERRA proceeding. In that decision, we stated that:

“... there are elements of reasonableness review within SOC 4. As we have previously stated, this is not a

traditional reasonableness review in that only certain aspects (contract administration and least cost dispatch) are subject to review in the ERRA, while other aspects (including terms and prices) are reviewed in the quarterly procurement advice letter process. However, with regard to least cost dispatch, we have no specified prudence or reasonableness evaluative criteria. We have instead stated that the utilities must use the most cost-effective mix of total resources, thereby minimizing the cost of delivering electric services. That is a compliance matter.” (D.05-01-054, p. 14, emphasis added.)

We went on to state that the least cost dispatch review process is a compliance review, and that there are no ranges of possible outcomes. (D.05-01-054, pp. 13-14.) Instead, we stated in pertinent part that:

“The outcome or standard for review has been predetermined – that is the lowest cost. SCE must demonstrate that it has complied with this standard, by providing sufficient information and/or analysis in order for the Commission to verify that SCE’s dispatch resulted in the most cost-effective mix of total resources, thereby minimizing the cost of delivering electric services. Based on analyses of SCE’s showing and subsequent discovery, ORA or any other party may take the position that SCE did not fully comply with SOC 4. In such cases, we will judge the merits of the parties’ positions and may impose disallowances and/or penalties.... This compliance process encompasses much more than that characterized by ORA. Imposing a compliance process for least-cost dispatch under SOC 4, rather than a reasonableness review process, does not diminish our ability to ensure just and reasonable rates.” (D.05-01-054, pp. 14-15.)

D.05-01-054 did not adopt specific criteria for determining “what constitutes least-cost dispatch compliance or what the utility needs to provide to meet its burden to prove such compliance.”¹³ (D.05-01-054, p. 15.) Instead, we stated that if ORA or another party can demonstrate that the utility “has not dispatched resources in a least-cost manner, the Commission will review that evidence and make appropriate adjustments for non-compliance.” (D.05-01-054, p. 16.)

ORA has not presented any new arguments in this proceeding that would cause us to reconsider the standard of review that we adopted for SCE in D.05-01-054. Accordingly, the same standard of review for least cost dispatch that we adopted in D.05-01-054 for SCE should also apply to the standard of review of PG&E’s least cost dispatch in its ERRA proceedings, i.e., a compliance review.

The standard of review of the contract administration is also that of a compliance review. As noted in D.05-01-054 at page 8, “SOC 4 is the upfront standard in a utility’s procurement plan regarding prudent contract administration and energy dispatch decisions.” Since § 454.5(d)(2) provides that an approved procurement plan shall eliminate the need for after-the-fact

¹³ We also stated that if specific criteria for determining what constitutes least-cost dispatch compliance are needed, that such criteria “should be developed in a generic proceeding where all affected utilities, as well as interested parties, could participate.” (D.05-01-054, p. 15.)

reasonableness reviews, the standard of review is to determine whether the utility's contract administration complied with the approved procurement plan.¹⁴

As for the standard of review that applies to URG-related costs, we stated in D.03-06-067 at page 10 that an inappropriate preference for URG resources is part of the least cost dispatch standard. Accordingly, a compliance review applies when URG is involved in least cost dispatch decisions. Although a compliance review applies, the utility is prohibited from any action that results in an inappropriate preference for URG resources or the utility's own negotiated contracts. (See D.05-01-054, p. 10; D.02-12-069, pp. 61-64.)

VI. Contract Administration, Procurement and Fuel Costs

A. Position of the Parties

1. PG&E

a) Contract Administration

The contracts that PG&E administered during the five-month record review period covered the allocated DWR contracts, qualifying facility (QF) contracts, other power purchase agreements, and new purchase contracts. Chapter 3 of Exhibits 100 and 101 discussed PG&E's administration of the contracts, and the processes that it utilized to fulfill its contract administration responsibilities.

Under the operating agreement between PG&E and DWR, which was approved in D.03-04-029, PG&E performs certain administrative functions

¹⁴ As noted in D.05-01-054, at p. 15, the compliance would consist of a showing of prudence for contract administration, for which the reasonable manager standard would apply.

with respect to the DWR contracts allocated to it. These functions include day-to-day scheduling and dispatch, managing fuel procurement, billing and settlements, and surplus power sales. To administer the allocated DWR contracts, PG&E formed a DWR contract administration function within PG&E's Gas and Electric Supply Department.

PG&E points out that ORA's testimony stated that "PG&E's QF power purchase contract administration and the payments made to QFs can be viewed as reasonable." (PG&E, Opening Brief, p. 3; Ex. 104.)

At page 3-8 of Exhibits 102 and 103, ORA stated that it could not determine whether PG&E's contract administration of the non-QF contracts was reasonable because PG&E did not provide ORA with sufficient information and data. PG&E believes that ORA reached this conclusion because ORA was "not physically present for every moment of dispatching and therefore can never say with complete certainty that they know that PG&E acted reasonably every moment of every day." (PG&E, Opening Brief, p. 4.) In Exhibit 105, PG&E states that "It is PG&E's understanding from discussions with ORA's project manager that ORA is not making any recommendations for disallowances or findings of unreasonableness in this phase of this proceeding, and is instead focused on improving the future transmission of data in a format and type that ORA believes to be more transparent."

Since PG&E and ORA have agreed to discuss what information and data should be provided to ORA in the future, and during "the record period, there were no instances of contracts not being administered in accordance with the terms of the contract, nor any contract disputes which were unreasonably resolved, per PUC Section 454.5(d)(2), and certainly no allegations of affiliate abuse, gross incompetence, fraud, abuse, or similar grounds, per

Section 454.5(h),” PG&E recommends that no findings of unreasonableness be made, that the record period be closed, and ORA’s request for additional data in future ERRA filings should be addressed. (Ex. 105, p. 3.)

Based on PG&E's description of its contract administration during the five-month record period, as contained in Exhibits 100 and 101, PG&E requests that the Commission find that PG&E:

“Reasonably administered its portfolio of DWR contracts and that all costs incurred under such agreements are recoverable in rates.

“Reasonably managed its QF and other PPAs and that all costs incurred under such agreements are recoverable in rates.

“Reasonably managed the renewable energy contracts and all costs incurred under such agreements are recoverable in rates.” (Exhibits 100 and 101, p. 3-32.)

b) Procurement Activities

Chapter 4 of Exhibits 100 and 101 describes the activities that PG&E undertook to procure sufficient energy supplies during the five-month record period to meet its customers' electric energy requirements. PG&E's 2003 procurement plan described how it planned to procure the necessary resources to meet its customer requirements, and the types of transactions it planned to engage in to manage its net open positions. The procurement plan also discussed the analyses it would use to assess its expected resource requirements, the tools that it would use, and the processes it would use to conduct the transactions. As described in PG&E's 2003 procurement plan, “the objectives of PG&E's electric procurement process are to ensure sufficient energy supply, reduce customer risk and maintain price stability at reasonable prices.”

(Exhibits 100 and 101, p. 4-1.) PG&E's resource requirements and its activities were evaluated by the Procurement Review Group (PRG).¹⁵

PG&E's procurement methods included using requests for offers, bilateral contracting agreements, exchange market transactions, and the Independent System Operator markets for energy and ancillary services. PG&E also participated in transactions to minimize potential transmission congestion penalty risks, and purchased firm transmission rights.

PG&E's procurement transactions were reported to the Commission's Energy Division on a quarterly basis through advice letter filings. The advice letter filings described the reasons for the transaction, the procurement process that was followed, and the quantitative assessment of the need for the transaction and its economic value to PG&E. For the transactions that PG&E engaged in from January through March 2003, PG&E filed electric Advice Letter 2377-E on May 1, 2003. For the transactions that took place from April through June 2003, PG&E filed electric Advice Letter 2402-E on July 15, 2003.

PG&E contends that during the record period, it procured electric energy resources and engaged in transactions in conformance with its 2003 procurement plan. PG&E used competitive energy markets whenever it was feasible, engaged in transactions that were designed to reduce costs to

¹⁵ The PRG was authorized by the Commission in D.02-08-071. The PRG's function is to consult with PG&E and review the details of PG&E's overall interim procurement strategy, the proposed procurement contracts, and the proposed procurement processes. (D.02-08-071, pp. 24-25.)

ratepayers, and provided detailed justification for all transactions in its quarterly electric advice letter filings.

c) Generation Fuel Costs

Chapter 5 of Exhibits 100 and 101 describes the actions that PG&E undertook to procure generation fuel for its URG plants, for the DWR contracts, hydroelectric facilities, and Diablo Canyon Power Plant (DCPP).

Based on PG&E's discussion of its generation fuel costs in Chapter 5 of Exhibits 100 and 101, PG&E requests that the Commission find that PG&E:

“Reasonably procured fuel for its retained generation facilities;

“Reasonably managed the provisions of the DWR tolling agreements consistent with the applicable Operating Order, Operating Agreement and/or Gas Supply Plan;

“Reasonably acquired water for hydroelectric generation; and

“Reasonably procured nuclear fuel for DCPP.”
(Exhibits 100 and 101, p. 5-19.)

PG&E also requests that the costs it incurred be recovered in rates.

2. ORA

a) Non-QF Contract Administration

Chapter 3 of ORA's report reviewed PG&E's contract administration activities for power purchase agreements, the allocated DWR contracts, and other miscellaneous contracts other than QF contracts. According to ORA, these contract administration activities “range from verification of

reported activities, to reconciling financial settlements, exercising options, negotiating amendments and checking for the completion of a variety of performance engineering tests.” (Exhibits 102 and 103, p. 3-1.) In addition, other activities include “reviewing fuel supply plans, forecast updates, and annual dispatch and availability reports as well as the surplus energy sales report.” (*Ibid.*) Each of the described activities also involves more specific tasks which ORA summarized at pages 3-1 to 3-2 of Exhibits 102 and 103.

ORA notes that the educational level and years of service for PG&E’s contract administration staff appear adequate for them to perform their duties. ORA also notes that the employee incentive plan does not explicitly link individual contract performance to work performed by specific employees, and that the incentive plan appears to mitigate conflicts of interest between the employee’s goals, and the overall departmental goals.

ORA recommends that PG&E be required to file advice letters for all contract amendments because of the potential financial impact on the contracts and the rate impact on ratepayers.

ORA also recommends that PG&E be required to provide a summary of all open and resolved dispute resolutions in future ERRA review applications. ORA believes that the summaries should include an economic impact analysis so that the economic effect on the contracts and ratepayers can be determined.

PG&E uses a “DWR Contract Administration Monthly Checklist” to manage the DWR contracts allocated to it. ORA recommends that several improvements be made to the checklist, as discussed at pages 3-5 to 3-6 and Attachment B of Exhibits 102 and 103. ORA believes its recommendations will

provide more controls and allow for better follow-up over the administration of the allocated DWR contracts.

ORA contends that during the five-month record period, PG&E had just begun to administer the DWR contracts, and that PG&E's contract administration manual for the DWR contracts was incomplete and still being developed. ORA states that the manual should contain "detailed methods for dispute resolution, standards and situational criteria," among other tools, in order to provide effective guidance. (Exhibits 102 and 103, p. 3-7.) ORA also believes that the manual should have "a thorough discussion of the contract administrator's job descriptions, the procedures to determine if a service provider is in compliance with its contract and, most importantly, an extensive list of protocols for dispute resolution." (*Ibid.*) ORA would also like the manual to "include oversight of current and forecasted supply and capacity, dispatch protocols, settlement issues and natural gas supply and pricing issues.

Without the additional information that ORA recommends be required, ORA states it cannot determine whether PG&E's contract administration of the non-QF contracts was reasonable.

b) QF Contract Administration and Costs

Chapter 4 of Exhibits 102 and 103 addressed ORA's "reasonableness review" of PG&E's QF costs during the five-month record period. During that period, PG&E purchased capacity and 7,682 GWh of energy from QFs for a total cost of \$608.6 million. As changed by Exhibit 104, ORA states in Exhibit 103:

"Based on ORA's review and analysis of PG&E's 2004 ERRR filing, workpapers and oral and written data request responses, PG&E's QF power purchase contract

administration and the payments made to QFs can be viewed as reasonable.” (Ex. 103, p. 4-1; Ex. 104.)

c) Procurement Activities and Fuel Costs

According to ORA's testimony, it "did not conduct a more comprehensive review of PG&E's procurement activities at this time because of ORA staff inexperience in ERRA proceedings and the paucity of information in PG&E's original filing." (Exhibits 102 and 103, p. 1-1.)

With respect to the review of PG&E's actions regarding generation fuel costs, ORA appears to have reviewed these costs as part of its review of the contract administration of the non-QF contracts.

ORA has not recommended any negative action with respect to PG&E's procurement or fuel cost activities during the record period.

B. Discussion

PG&E's updated 2003 procurement plan described its projected 2003 requirements and the timing and type of actions it planned to take to meet these requirements. The procurement plan also described risk management and credit management activities, and proposed benchmarks for the Commission to use in determining whether PG&E achieved its procurement goals.

In its testimony in this proceeding, PG&E described its contract administration, procurement activities, and generation fuel procurement. PG&E also met with ORA on a number of occasions to discuss PG&E's activities during the record period. ORA undertook a review of PG&E's activities during the record period as described in its testimony.

With regard to PG&E's contract administration for non-QF energy resources, ORA made several recommendations as to the type of information that PG&E should supply and how PG&E's management of the DWR contracts could be improved. Although ORA does not recommend any disallowance for administration of these contracts, ORA states in Exhibit 103 at page 3-8 that "In

the absence of the above-information and based on the information provide[d] by PG&E in its Testimony, ORA cannot determine whether its contract administration is reasonable.”

For PG&E’s contract administration of the QF contracts, ORA states in Exhibit 104 that “Based on ORA’s review and analysis of PG&E’s 2004 ERRA filing, workpapers and oral and written data request responses, PG&E’s QF power purchase contract administration and the payments made to QFs **can** be viewed as reasonable.” (Original emphasis.)

We have reviewed the testimony of both PG&E and ORA regarding contract administration, procurement activities, and generation fuel procurement for the five-month record period.

In PG&E’s rebuttal testimony, PG&E responded to ORA’s recommendations regarding the contract amendments, contract disputes, contract administration oversight of the DWR contracts, and the contract administration manual. PG&E pointed out the differences between contract amendments which have an immediate and direct impact on ratepayers and contract amendments that only tangentially affect ratepayers, and contract disputes which are non-routine in nature and contract disputes that are minor or routine. PG&E also notes that it has replaced the “DWR Contract Administration Monthly Checklist” with a compliance tracking system that addresses ORA’s concerns regarding the checklist. PG&E also uses its Qualifying Facilities Information System to track, manage and pay the QFs. PG&E also states that “Given the disparate nature of the various contracts, PG&E does not have a formal contract administration manual that attempts to cover every possible situation that may arise in either the contracting or contract administration process.” (Ex. 105, p. 12.) Instead, the various PG&E groups which oversee the

administration of these various contracts use a collection of contract administration and settlement responsibilities, which PG&E can provide as part of the response to a master data request.

Although ORA states at page 3-8 of Exhibit 103 that ORA could not determine whether PG&E's contract administration of the non-QF contracts was reasonable, PG&E's understanding of that reference is "ORA is neither asking that this phase of the proceeding remain open for further investigation nor for a finding of unreasonableness." (Ex. 105, p. 1, fn. 1.) Instead, "it is PG&E's understanding that ORA's recommendations in Chapter 3 asks that additional data be provided in future ERRA proceedings." (*Ibid.*) Since it appears that ORA is not requesting that PG&E's reasonableness of its contract administration be determined in a separate phase, and because ORA has not requested that PG&E's contract administration be found unreasonable, we address PG&E's contract administration for the record period in this decision.

Based on ORA's review of PG&E's contract administration, procurement activities, and generation fuel procurement, the testimony of both PG&E and ORA, and since there are no recommendations for disallowances of findings of unreasonableness, we find as follows for the period of January 1, 2003 through May 31, 2003:

1. PG&E reasonably administered its portfolio of the DWR contracts allocated to it in compliance with its 2003 procurement plan, and all costs incurred under such agreements are recoverable in rates.
2. PG&E reasonably managed its QF contracts and other purchase power agreements in compliance with its 2003 procurement plan, and all costs incurred under such agreements are recoverable in rates.

3. PG&E reasonably managed its renewable energy contracts in compliance with its 2003 procurement plan, and all costs incurred under such agreements are recoverable in rates.
4. PG&E's procurement of energy and energy transactions were in compliance with its 2003 procurement plan.
5. PG&E reasonably procured fuel for its retained generation facilities in compliance with its 2003 procurement plan, and all of the associated costs are recoverable in rates.
6. PG&E reasonably managed the provisions of the DWR tolling agreements in compliance with the applicable Operating Order, Operating Agreement, and/or Gas Supply Plan, and all of the associated costs are recoverable in rates.
7. PG&E reasonably acquired water for hydroelectric generation in compliance with its 2003 procurement plan, and all of the associated costs are recoverable in rates.
8. PG&E reasonably procured nuclear fuel for DCPP in compliance with its 2003 procurement plan, and all of the associated costs are recoverable in rates.

VII. Least Cost Dispatch

A. Position of the Parties

1. PG&E

PG&E's least cost dispatch process is described in Chapter 2 of Exhibits 100 and 101. PG&E's least cost dispatch in 2003 utilized existing generation and contracts, the DWR allocated contracts, market opportunities for

energy purchases and sales, and gas procurement to support the dispatch of PG&E's electric supply portfolio.

According to PG&E, no preference was given to PG&E's URG resources. Instead, PG&E's least cost dispatch involved the dispatch of resources or the purchasing of energy with the lowest incremental cost of providing energy.¹⁶ PG&E asserts that this approach is consistent with SOC 4 in D.02-10-062 and D.02-12-069, which states "the utilities shall prudently administer all contracts and generation resources and dispatch the energy in a least cost manner," and also prohibits any action that results in a preference to URG resources or the utility's own negotiated contracts. (Exhibits 100 and 101, pp. 2-2, 2-14; D.02-10-062, pp. 52, 74; D.02-12-069, pp. 64, 70.)

To carry out least cost dispatch, decisions are made using the best information available at the time. Load, weather, system conditions, and market prices are all factors which affect the dispatch decision. Hydro conditions and plant outages need to be considered in the planning process, and span multiple months and years. PG&E engages in "a series of ongoing analyses and activities that focus on different timeframes and decisions." (Exhibits 100 and 101, p. 2-9.) PG&E performs and updates its assessments of its net open position on a regular basis to determine whether additional resources are required or if it has excess resources for potential surplus sales. By performing updates, PG&E ensures that it has the resources to meet its requirements. The assessments which PG&E

¹⁶ The only exception to this least cost dispatch approach is the dispatch of hydroelectric resources. PG&E states that it may be more prudent to defer hydroelectric generation to higher value periods because of the future value of water and the fact that available water is limited.

undertakes are summarized in Attachment 2-1 of Exhibits 100 and 101 at pages 2-16 to 2-17.

PG&E's testimony notes that sometimes operational, physical, legal, regulatory, environmental, and safety constraints result in a departure from a pure economic dispatch of PG&E's resources. Due to these constraints, the dispatch decision involves more than just comparing the operating costs of various resources and market prices. PG&E developed a least cost dispatch approach which incorporates these resource constraints and incremental costs, and which is described at pages 2-7 to 2-8 of Exhibits 100 and 101.

PG&E asserts that its testimony in Exhibits 100 and 101 demonstrates that it has complied with all of the least cost dispatch mandates described in D.02-10-62, D.02-12-069, D.02-12-074, and D.02-09-053. PG&E also points out that ORA's testimony "does not recommend any disallowances related to least cost dispatch at this time." (PG&E, Opening Brief, p. 3; Exhibits 102 and 103, p. 2-1.) PG&E requests that the Commission find that:

"PG&E prudently administered all contracts and generation resources and dispatched energy in a least cost manner;

"Consistent with the Commission's direction, PG&E's economic dispatch during the record period made no distinction between its own resources; contracted resources; market transactions (both purchases and sales) and DWR allocated contracts in its dispatch decisions; and

"All resources were dispatched based on their incremental costs, recognizing all operating constraints and all regulatory, environmental, and legal obligations." (Exhibits 100 and 101, p. 2-15.)

2. ORA

ORA met with PG&E personnel and reviewed the information listed at pages 2-3 to 2-4 of Exhibits 102 and 103 as part of its review of the record period. ORA also reviewed PG&E's hourly data from one-day in each month of the record period to determine whether PG&E followed least cost dispatch principles. ORA did not find any deviations from these principles.

ORA asserts that although PG&E's testimony explained the process that it would utilize to minimize the cost of resources to the ratepayers, PG&E did not make a showing that it minimized costs to ratepayers during the record period, and it "failed to provide least cost dispatch information in a manner that facilitated ORA's review." (Exhibits 102 and 103, pp. 2-4 to 2-5.) ORA had to review a sampling of data in order to determine whether PG&E complied with the least cost dispatch requirements. ORA states that this resulted in a very difficult and time-consuming process.

ORA recommends that until a "more efficient method is developed to determine the reasonableness of least cost resource utilization," that PG&E provide the information listed at pages 2-4 to 2-5 of Exhibits 102 and 103 "in all subsequent ERRA reasonableness filings to facilitate the review process," and that "PG&E should provide the information in a format that clearly shows that least cost dispatch was achieved. (Exhibits 102 and 103, pp. 2-4 to 2-6.)

Based on its analysis, ORA does not recommend any disallowances relating to PG&E's least cost dispatch at this time. To facilitate an effective review of PG&E's least cost dispatch, ORA recommends that PG&E be required to provide the information described at pages 2-4 to 2-5 of Exhibits 102 and 103 in future ERRA filings.

B. Discussion

We addressed the appropriate scope of review for least cost dispatch earlier in this decision.

ORA did not recommend any disallowances related to least cost dispatch. ORA did, however, recommend in its testimony that PG&E provide more detailed information pertaining to least cost dispatch. (See Ex. 102 and 103, pp. 2-4 to 2-5.) The master data request section of this decision addresses ORA's request for this information.

Based on ORA's review of PG&E's least cost dispatch, ORA's sampling of data, the testimony of both PG&E and ORA, and no recommendations for disallowances, we find as follows for the period of January 1, 2003 through May 31, 2003:

1. PG&E reasonably administered all contracts and generation resources and dispatched energy in a least cost manner.
2. PG&E's economic dispatch decisions during the record period made no distinction between its own resources, contracted reserves, market transactions (both purchases and sales), and the allocated DWR contracts.
3. PG&E dispatched all resources based on their incremental costs, while recognizing all operating constraints and all regulatory, environmental and legal obligations.

Having reviewed PG&E's ERRA-related activities for the five-month record period, this record review period is closed.

VIII. Master Data Request**A. Position of the Parties****1. PG&E**

ORA's Exhibits 102 and 103 list the kind of information ORA would like to receive in future ERRR filings so that it can effectively review the utility's contract administration and least cost dispatch. ORA's testimony acknowledges that it is still in the process of developing the most efficient and effective method of conducting the ERRR review, and anticipates that the process will improve over time. PG&E states that it has been working with ORA's representatives on the data that PG&E has available and what it can provide to ORA in the context of ORA's requests. ORA's testimony acknowledges the many hours that PG&E's staff has met with ORA to understand PG&E's processes and decision making. PG&E and ORA have agreed that a master data request should be used as a regular part of the ERRR review process. (See PHC R.T., pp. 16, 18.) PG&E states that it is willing to work with ORA to adjust the "data to meet ORA's perceptions of what it needs to conduct an efficient and effective review." (Ex. 105, p. 2.)

PG&E contends that the specific data to be included in the master data request should not be established in a Commission decision. According to PG&E, it makes little sense to force a utility to provide specific data when that data may no longer be useful or desirable to those assigned to review the utility's showing.

Since there is no controversy over the master data request, PG&E asserts that there is no need to address the master data request in this proceeding. In the alternative, the decision should simply note that PG&E and

ORA have agreed that additional specific data needs will be addressed through a master data request in future ERRA filings.

2. ORA

ORA states in its reply brief that it agrees with PG&E that the decision in this proceeding should note that the two have agreed that ORA's requests for specific data and information for the review of PG&E's procurement costs will be addressed through a master data request in future ERRA filings.

B. Discussion

ORA made a series of recommendations regarding the type of information that PG&E should supply as part of the review of the ERRA activities. ORA's testimony and PG&E's rebuttal testimony spent a lot of time addressing the type of data and information that ORA would like to have. Although PG&E does not believe that ORA needs all of the data and information that ORA has requested, PG&E is willing to work with ORA to determine how it can satisfy ORA's informational needs.

Instead of deciding in this decision the specific type of information that PG&E should provide to ORA, we favor the approach that ORA and PG&E appear to agree upon. Instead of adopting a standardized master data request for the review of the ERRA activities for the designated record period as part of this decision, ORA and PG&E appear willing to work out the type of information that should be supplied in future ERRA reviews. Since the ERRA review process is still evolving, the details of what information should be provided to ORA are best left to ORA and PG&E to work out.¹⁷ ORA and PG&E should discuss

¹⁷ Similar approaches were adopted for SCE in D.05-01-054 and D.05-02-006.

among themselves the type of information and data that ORA needs, and which PG&E can supply so that an efficient and timely review of the ERRA activities for the record period can occur. Both sides also need to consider each other's needs and the limitations of how useful the requested information will be and whether the information can be readily supplied. If a dispute arises over the kind of information to be provided to ORA, the parties can bring the dispute to our attention for a resolution.

IX. Comments on Draft Decision

The draft decision of the ALJ in this matter was mailed to the parties in accordance with § 311(g)(1) of the Public Utilities Code and Rule 77.7 of the Rules of Practice and Procedure. Comments to the draft decision may be filed in accordance with Rule 77.7.

X. Assignment of Proceeding

Michael R. Peevey is the Assigned Commissioner and John S. Wong is the assigned ALJ in this proceeding.

Findings of Fact

1. The ERRA balancing account was established to record and recover the utilities' energy procurement plan power costs.
2. PG&E's updated procurement plan for 2003 was approved in D.02-12-074.
3. At the May 3, 2004 prehearing conference, PG&E and ORA agreed that evidentiary hearings were not needed.
4. ORA's review of PG&E's ERRA-related activities for the five-month record period of January 1, 2003 through May 31, 2003 does not recommend any disallowances or findings of unreasonableness.

5. The scope of review of least cost dispatch should be addressed in this proceeding so that PG&E and ORA have guidance in future ERRA proceedings regarding the review of PG&E's dispatch activities.

6. Section 454.5(b) provides that the procurement plan is to include upfront standards and criteria by which the acceptability and eligibility for rate recovery of a proposed procurement transaction will be known by the electrical corporation prior to execution of the transaction.

7. The same scope of review of least cost dispatch that was adopted in A.03-10-022 should also apply to PG&E's ERRA proceeding.

8. PG&E reasonably administered its portfolio of the allocated DWR contracts in compliance with PG&E's 2003 procurement plan.

9. PG&E reasonably managed its QF contracts and other purchase power agreements in compliance with its 2003 procurement plan.

10. PG&E reasonably managed its renewable energy contracts in compliance with its 2003 procurement plan.

11. PG&E's procurement of energy and energy transactions were in compliance with its 2003 procurement plan.

12. PG&E reasonably procured fuel for its retained generation facilities in compliance with its 2003 procurement plan.

13. PG&E reasonably managed the provisions of the DWR tolling agreements in compliance with the applicable Operating Order, Operating Agreement, and/or Gas Supply Plan.

14. PG&E reasonably acquired water for hydroelectric generation in compliance with its 2003 procurement plan.

15. PG&E reasonably procured nuclear fuel for DCPP in compliance with its 2003 procurement plan.

16. PG&E reasonably administered all contracts and generation and dispatched energy in a least cost manner.

17. PG&E's least cost dispatch decisions during the record period made no distinction between its URG, contracted reserves, market transactions, and the allocated DWR contracts.

18. PG&E dispatched all resources based on their incremental costs, while recognizing all operating constraints and all regulatory, environmental and legal obligations.

19. The five-month record review period of PG&E's ERRA-related activities is closed.

20. Since the ERRA review process is still evolving, the details of what information should be provided to ORA are best left to ORA and PG&E to work out.

Conclusions of Law

1. SOC 4 is an upfront standard and criteria which provides that the utilities shall prudently administer all contracts and generation resources and dispatch the energy in a least-cost manner.

2. Since least cost dispatch is part of the contract administration, SOC 4 does not allow the Commission to conduct an after-the-fact reasonableness review of the terms or prices of the contracts.

3. A review of least cost dispatch is permitted under § 454.5.

4. The same scope of review of least cost dispatch that was adopted in A.03-10-022 should also apply to PG&E's ERRA proceeding.

5. PG&E's decisions to dispatch the resources under its control in the daily, hourly and real-time markets are relevant to the ERRA review.

6. A compliance review, which is the same standard of review that was adopted in A.03-10-022, should also apply to PG&E's ERRA proceeding.

7. Although a compliance review applies to least cost dispatch decisions, the utility is prohibited from any action that results in an inappropriate preference for URG resources or the utility's own negotiated contracts.

8. PG&E should be allowed to recover in rates all of the costs that it incurred in connection with its contract administration, fuel costs, the DWR tolling agreements, water purchases for hydroelectric generation, and for the purchase of nuclear fuel.

9. ORA and PG&E should discuss the type of information and data that ORA needs, and which PG&E can supply, so that an efficient and timely review of the ERRA activities can occur.

O R D E R

IT IS ORDERED that:

1. To the extent existing rates do not fully recover the costs associated with the Energy Resource Recovery Account (ERRA) activities discussed in this decision, Pacific Gas and Electric Company (PG&E) may adjust its ERRA rates to recover those costs.

2. PG&E and the Office of Ratepayer Advocates (ORA) shall develop and implement a master data request process to be used in PG&E's future ERRA filings.

If PG&E and ORA are unable to agree on the kind of information to be provided to ORA, PG&E and ORA may bring the dispute to our attention for a resolution.

3. This proceeding remains open to address the seven-month review period.

This order is effective today.

Dated _____, at San Francisco, California.